Mobile Money
for the Unbanked

Setting up shop: Strategies for building effective merchant payment networks

Findings based on the State of the Industry Report

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For mobile money providers, merchant payments have huge potential to increase mobile money transaction volumes. As a product, merchant payments have caught the attention of mobile money providers because of the sheer magnitude of retail payments in the market and the opportunity it represents to integrate the mobile wallet more deeply into everyday life. In 2012, 28 mobile money services were offering merchant payments. Two years on, 60 services have rolled out merchant payments, but only a handful are generating over 1,000 transactions a month.

This publication is part of a series of deeper insights into selected topics based on the findings of the 2013 State of the Industry Report on Mobile Financial Services. Sixty of the 98 mobile money providers surveyed offered merchant payments, with 28 planning to launch the product in the next 12 months. Merchant payments accounted for 1.6% of total transaction volumes and 4% of total transaction values in June 2013.[1]

To gain a better understanding of approaches to merchant acquisition and management, MMU conducted 12 interviews with mobile money deployments that have made significant strides in building a merchant network. The interviews covered mobile money services across Latin America, Sub-Saharan Africa, Middle East and North Africa, South Asia, and East Asia and Pacific.

MERCHANT PAYMENTS AT A GLANCE[2]

60 SERVICES OFFERED MERCHANT PAYMENTS

53K REGISTERED MERCHANTS

12K ACTIVE MERCHANTS (30 DAYS)

5.1 MILLION TRANSACTIONS (VOLUME)

USD 128.2 MILLION IN TRANSACTIONS (VALUE)

SUMMARY

Building an active merchant network is no small feat. It requires substantial investments in human capital and marketing, as well as laser-sharp focus from the management team. It is potentially as difficult as building an agent network, and operators must choose whether to do this themselves or work with specialised merchant acquirers. To ensure quality, it is important to segment and target the right merchants and create an appropriate commission structure for sales representatives. Finally, creating a compelling merchant proposition requires holistic thinking about the point-of-sale experience, pricing, settlement, and service reliability.

1. Claire Pénicaud and Arunjay Katakam (2014), "State of the Industry 2013: Mobile Financial Services for the Unbanked", http://www.gsma.com/mobilefordevelopment/wp-content/uploads/2014/02/SOTIR_2013.pdf
2. Data as of June 2013.

To be successful in merchant payments, mobile money services must adopt a comprehensive and strategic approach to segmenting, targeting and acquiring merchants, and then successfully manage those merchants on an ongoing basis. This publication examines the challenges mobile money providers face and sheds light on the various strategies successful providers have used to acquire and manage their merchant networks.

In October 2012, the GSMA published a paper on eWallet merchant payments[3] that discusses the opportunities, necessary conditions, a pricing models, and technology considerations involved in deploying a merchant payments network.

Things to consider before you begin

1. **Take local market conditions into account.** Mobile money providers have taken a wide range of approaches to rolling out merchant payments in their markets. In Latin America, companion cards are popular. Four services in the region offering merchant payments issue companion cards to their customers, leveraging the existing payment card industry infrastructure. In Africa, where card payments are less common, most merchants are issued a special SIM card dedicated for merchant payments, and in some cases a free phone to go with it. One service interviewed in South Asia issues its larger merchants a point-of-sale (POS) terminal to provide customers with a receipt. Another service in East Asia and Pacific is planning to enhance its product offering by providing merchants with a smartphone and mPOS (mobile point-of-sale) dongle, enabling them to accept credit and debit card payments.

2. **Customers need to have money regularly flowing into their mobile wallet.** This can happen in two ways:

   a. The mobile money service is mature and customers use mobile money a lot, trust it, and are comfortable leaving a balance in their mobile wallet.

   b. Mobile money customers regularly receive significant amounts of money in their wallet, either from bulk payments (e.g. a monthly salary), transfers from bank accounts, or even international remittances.

3. **Merchants need to be able to make payments to their suppliers.** It is problematic for merchants to receive a substantial portion of their takings in mobile money if suppliers need to be paid in cash.

Once a service provider selects a model that fits the local market, it will need to devise a strategy to manage its merchant network as it expands over time. The following two sections explore some successful approaches mobile money providers have taken in these areas.

3. M. Yasmina McCarty (2012), "eWallet Merchant Payments: GSMA Discussion Paper", http://www.gsma.com/mobilefordevelopment/wp-content/uploads/2012/10/2012_MMU_eWallet-Merchant-Payments1.pdf

Building a merchant network

Building an active merchant network requires significant investments. All of the mobile money providers MMU interviewed admitted rolling out merchant payments was more challenging than they had anticipated, with some saying they had found it just as difficult as building their agent network. Some of the main lessons and insights from mobile money providers about how to build a merchant network are described in this section.

> *"Frankly it is going to be a lot of work on our part to drive behaviour change, however we think it is worth the effort."*
> – MTN Uganda

Merchant networks need to be larger than agent networks. The potential number of merchant payments a customer will make with their mobile account is far greater than the number of transactions they would make at an agent. For example, in a single week, a customer might purchase groceries, visit a pharmacy and eat at a restaurant, but only visit their agent once to cash-in or cash-out. Therefore, providers seeking to build an effective merchant payments network will need to recruit more merchants than agents to create a sustainable ecosystem of businesses using mobile money.

Dedicated teams have been built to sign up merchants. Mobile money providers that used the same recruitment team for both agents and merchants found its team spent less time signing up merchants, often because they were more familiar with agent recruitment and there were already established practises in place for signing up agents. Ultimately, 10 of the 12 services created a dedicated sales force to sign up merchants.

Both quality and quantity are important when signing up merchants. Active merchant rates (the percentage of merchants transacting on a monthly basis) can suffer when operators focus on signing up as many merchants as possible. **A lot depends on the commission structure of the sales force hired to acquire merchants.** If a commission is paid for every merchant acquired, this tends to result in many inactive merchants, whereas a staggered commission structure that rewards transaction volumes rather than sign-ups is likely to produce a larger percentage of active merchants. Kenya's Safaricom (see Box 1) and Kopo Kopo have both found this to be the case (see Box 3).

BOX 1

SAFARICOM'S MERCHANT ACQUISITION COMMISSION STRUCTURE

Safaricom adopted a tiered model for its introducers' commission structure, designed to reward direct sales representatives who introduced merchants that would promote its Lipa na M-PESA merchant payments service through regular customer use. However, since subsequent payments were dependent on the merchant achieving certain transaction thresholds, many of the DSRs took the first payment and moved on to signing up the next merchant, never advancing beyond the first tier. This resulted in high acquisition rates, but lower active usage rates. This is reflected in Safaricom's March 2014 results, which reported 122,000 registered merchants and 24,137 active merchants[4] with an active merchant rate of 19.8 percent. While staggered commission structures are more likely to yield a larger number of active merchants, the structure must be appealing for sales representatives to move up the tiers.

Effective segmentation, prioritisation, and targeting of merchant segments are key to success.[5] Interviews with mobile money providers revealed two illustrative examples. One service used the top ten merchant category codes (MCC) in the United States and Europe to inform its strategy, and later found that transaction volumes followed a similar pattern in its own market. Another service targeted merchants with more than one employee; absentee owners found electronic transactions were a good way to track their business and prevent till theft by employees.

4. Safaricom Limited FY14 Presentation (2014), http://www.safaricom.co.ke/images/Downloads/Resources_Downloads/FY_2014_Results_Presentation.pdf
5. A detailed analysis of segmentation can be found in: M. Yasmina McCarty (2012), "eWallet Merchant Payments: GSMA Discussion Paper", http://www.gsma.com/mobilefordevelopment/wp-content/uploads/2012/10/2012_MMU_eWallet-Merchant-Payments1.pdf

Persuading merchants to sign up depends on finding the right pricing model. Many merchants may not be familiar with the payment card industry's merchant discount rate (a fee charged to merchants for processing card-based electronic transactions), and often questioned the value of paying a fee to accept mobile money payments. Regardless of whether the merchant or the customer has to pay for the transaction, the additional cost tends to be met with resistance. Where merchants are also agents, they lose income (cash-out fee) and then incur a transaction fee. Some providers are considering a no-cost transaction model, as they believe it would provide the impetus required to keep the funds within their mobile money ecosystem (reducing total cash-outs).

Educating merchants on the benefits of mobile money was consistently reported to be one of the biggest challenges in acquiring merchants. Intangible benefits, such as reducing the cost of cash in their business or the ability to enhance their credit score for working capital loans, are more difficult for merchants to accept. A number of the mobile money providers interviewed said they adapted their pricing models, provided free phones, and used other incentives to help convince merchants. It may be too early to tell whether these tactics have been effective, but the providers recognise the importance of trying different strategies and early signs are encouraging.

Using partnerships to build merchant networks has proved to be very effective for the payment card industry. Mobile money providers need to decide whether they want to partner with third-party merchant acquirers and/or use an in-house team (see Figure 1 and Table 1 below). Whereas most services launched to date have used in-house distribution teams to acquire merchants, Safaricom partnered with Kopo Kopo to enrol merchants to accept M-PESA in Kenya (see Box 3).

FIGURE 1
PARTNERSHIP MODEL FOR MERCHANT NETWORK ACQUISITION

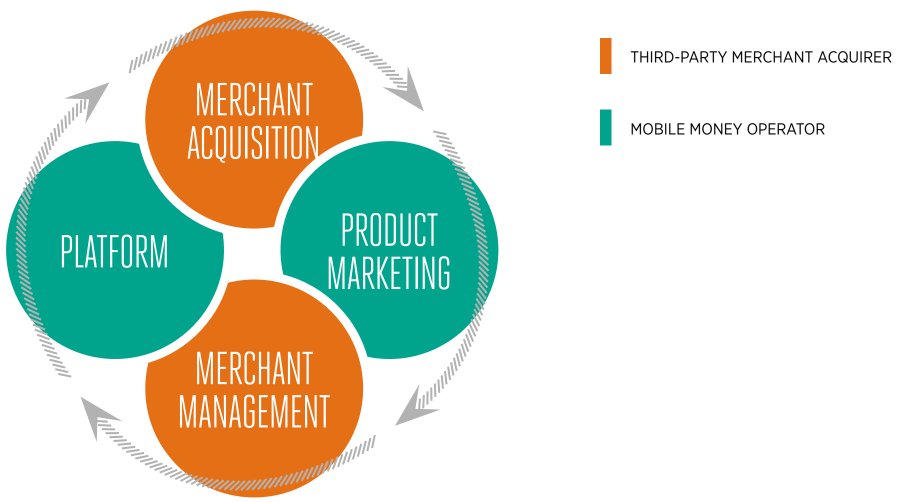

TABLE 1
BENEFITS AND LIMITATIONS OF USING A THIRD-PARTY MERCHANT ACQUIRER

BENEFITS	LIMITATIONS
+ Services focus on their strong points	– Lack of control over merchants
+ Quality merchants are signed up since partner revenue is dependent on transactions	– Reduced revenue due to revenue sharing
+ Leverage the ability of experienced partners to deliver results	– Partner selection and incentive alignment can be a risk

Managing a merchant network

Relatively speaking, signing up a merchant is the easy part; managing a merchant network on an ongoing basis requires significant resources. If it does not cost a merchant anything to sign up, most will do so, even if they are not yet fully convinced of the benefits. In most pricing models, merchants begin paying for the service when they transact, which is when cracks can start to appear. Merchants need to be visited frequently to reinforce the value proposition and ensure they are comfortable using the service. This helps resolve any challenges the merchant faces, which may not be otherwise brought to the service provider's attention.

All of the providers reported providing training to merchants they had acquired and have a dedicated helpline for support, but inactive merchant rates are a problem for every service at some stage. Two services, Telesom's ZAAD in Somaliland and Kopo Kopo in Kenya, have overcome this issue and it is worth understanding how they did it.

BOX 2

ZAAD, TELESOM SOMALILAND

As of June 2014, ZAAD had 12,300 registered merchants with an active rate of 89%, compared with 35% in their first year after launch.

Telesom began by focusing its merchant acquisition on major reputable business, visiting them and marketing directly to decision-makers. At the start, merchants would sign up to Telesom's mobile money transfer service, ZAAD, but not transact (thus becoming inactive). Telesom also noticed that merchants were using their customer account, not their merchant account, to accept payments.

Telesom reached out to inactive merchants, asking them directly why they were not using their merchant accounts and what challenges they had experienced. Merchants reported limitations with the service, such as only being able to cash-out at ZAAD retail stores and not perform any other transactions (e.g. P2P or bill payment). This left merchants with limited ability to access their funds when they needed to, which created a liquidity problem as they did not have cash available to pay their suppliers. Based on their feedback, Telesom built three new features:

1. M2M (merchant-to-merchant) transfers allowing merchants to buy from their suppliers;
2. M2P (merchant-to-person) transfers allowing merchants to make personal payments; and
3. Interconnection with Salam Bank automatically depositing at the bank on a daily basis, with no need for an in-person visit.

These three features improved liquidity for the merchants and vastly increased their activity rates. The total number of businesses using mobile money on a regular basis also increased as suppliers chose to join the network.

BOX 3
KOPO KOPO, KENYA

In its first year, Kopo Kopo, a merchant services company employed by Safaricom, was rapidly signing up merchants and quickly realised that activity rates (which were around 10%) were not what it expected them to be. That's when the company decided to slow down the process and think about two important questions.

- **Who do we acquire?** Using a market segmentation approach, the Kopo Kopo team figured out which merchants had the strongest pain points mobile money could solve and targeted those merchants first.
- **How do we acquire?** By changing the commission structure for direct sales representatives to a two-tier model, Kopo Kopo rewarded both merchant sign-up and activity. Finally, it improved the logistics of its merchant sign-ups by using a tracker to inform merchants where they were in the approval process. Kopo Kopo found this tracker also helped merchants remember what they signed up for.

The results showed that, on a monthly basis, Kopo Kopo went from signing up 2,000 merchants with a 30-day activity rate of 10% (200 active merchants) to 500 merchants with a 30-day activity rate of 40% (200 active merchants). By quadrupling their active rate, they had reduced their acquisition cost per merchant, yet maintained the same revenue from merchant transactions. In addition, Kopo Kopo introduced a new product called Kopo Kopo Grow, which provides merchants with a cash advance service to replenish stock, refurbish their premises, or launch a new business line. Repayments are based on electronic sales and Kopo Kopo Grow aligns perfectly with cash flow: Kopo Kopo deducts a larger amount when sales are high, a smaller amount when sales are low, and nothing when there are no sales.

In addition to the above examples, other providers have found the following practises to be instrumental in increasing merchant activity rates:

Successful mobile money providers use an internal dashboard to review merchant activity on a regular basis. This helps providers understand how many merchants are active, what makes them active, what is driving the transaction volumes, what types of businesses are most active, and other insights such as peak transaction times (day or night). Using this data, providers can tweak their merchant reactivation strategy.

Merchants with an interest in analysing how their business is performing or need to perform reconciliations require access to transaction data outside of USSD and SMS. Providing merchants with web-based access to transaction reports is important. Having to go through hundreds of SMS messages at the end of the day to tally transactions will not motivate merchants to use the service. Giving them the tools to manage their businesses through their transactions will likely see merchant activity rates improve.

The settlement process is a critical factor in getting merchants to use the service. Providing merchants with clarity around settlement and how to access their funds is important to making them feel comfortable with the service. Merchants typically have limited cash flow and need to use the proceeds from sales for restocking (paying suppliers) on a daily basis. Asking the merchant to cash-out every day is not convenient or practical, often due to withdrawal limits. Merchants need to be able to access their funds quickly; otherwise, they simply will not use the service.

The reliability of the service is crucial. In one example shared by an interviewee, a bar fight broke out when a service was down for scheduled maintenance at 2 a.m. Two of the twelve services identified delays in merchants receiving SMS confirmations as a common problem, and one said that sometimes a merchant's inbox is full and no new SMS messages can be delivered.

Visiting merchants regularly to ensure they are trained and have their phone/POS available and charged when a customer comes to transact helps to drive transactions and merchant activity. However, transaction speed was not identified as a barrier for most merchant segments. Although technology can and will be improved, it currently does not appear to be the primary reason why transaction volumes or merchant active rates are low.

Above all, merchants must be given a complete experience. Similar to the complexities of managing an agent network (such as education, training, and liquidity management), mobile money providers need to provide merchants with the full range of tools and support they need to succeed. Simply giving them a phone and putting a sticker on their door is not enough; they need to be provided with a complete package of initial and ongoing training, as well as effective management.

Conclusion

Merchant payments have the potential to increase mobile money transaction volumes by an order of magnitude. While mobile money providers seem to recognise the opportunity of allowing merchant payments via mobile money, adoption has not yet met their expectations. Today, merchant payment numbers are significant for only a handful of services and are struggling to gain traction in most cases.

Mobile money providers need to invest significant resources in merchant acquisition or partner with specialists to build an active merchant network. Focused and dedicated teams with specific skills are needed to educate and convince merchants to use the service. A strong value proposition is essential to hold merchants' interest and deliver sustainable transaction volumes. Using segmentation to attract the right merchants with an appropriate commission structure will help build a quality merchant network. Providing merchants with a complete experience (fast settlement and access to their transaction data) will increase their confidence in the system.

Real success in merchant payments will come when a service has managed to create an entire ecosystem. Simply signing up merchants is not a formula for success; it is the transactions that count. Having funds in mobile money accounts is a prerequisite, but customers will not cash-in to pay a merchant unless they are able to clearly see the benefit of doing this for multiple activities in their daily life. Similar to ZAAD's approach, developing products such as bulk payments and integrating with banks will go a long way towards injecting funds into the mobile money ecosystem.

Finally, a word of caution: Different strategies are required for different market conditions. Local market conditions will require different prioritisation of merchant and customer segments, pricing and POS models, and acquisition models, among other factors. This requires complex decisions from mobile money providers to navigate these conditions, and the flexibility to adapt to meet merchant needs. Simply replicating what others have done without tailoring strategies to one's own context will not suffice in the long run, but putting the right effort in from the start will help the service grow and reach scale.

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